



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

Number: **201230026**  
Release Date: 7/27/2012

Date: May 4, 2012

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

UIL: 507.01-00, 4940.00-00, 4941.00-00, 4942.00-00,  
4944.00-00, 4945.00-00

Legend:

Foundations =

Dear :

This is in response to your ruling request regarding the proper treatment of a transfer of all of your net assets to other private foundations under §§ 507, 4940, 4941, 4942, 4943, 4944, and 4945 of the Internal Revenue Code (Code).

**Facts:**

You are a newly formed organization that is recognized as exempt from federal tax under § 501(c)(3) and are classified as a private foundation under § 509(a). You expect to receive assets in fulfillment of a bequest from a marital trust and annual payments from two charitable lead unitrusts which are split-interest trusts described in § 4947(a)(2). Your directors have different charitable philosophies and divergent charitable goals, and they believe that their charitable endeavors will be more efficiently managed through two separate foundations that are also recognized as exempt under § 501(c)(3) and classified as private foundations under § 509(a). To accomplish this objective, you propose to transfer, pro rata, approximately two thirds of your assets to one of the Foundations and the remaining one third of your assets to the other foundation. Together, both transfers will constitute all of the assets to be received from the marital trust. The transfers will be for no consideration and not out of current income. In addition, the charitable lead unitrusts will modify the terms of their agreements to designate the Foundations as their charitable lead beneficiaries, instead of you. You and the Foundations are not, and will not be, operating foundations within the meaning of § 4942(j)(3).

You have three directors, all of whom are siblings. Two of those siblings and their spouses govern one transferee foundation, and the third sibling, his spouse, and their child govern the other transferee foundation. Your board proposes to transfer all of your assets to the Foundations immediately upon receipt of the distribution from the marital trust. You will obtain an order of a state court of jurisdiction approving the transfers and the associated restructuring. After completion of the transfers, you will not have any assets. Not earlier than one day after final distribution of your net assets, you will provide voluntary notice to the Secretary of your intention to terminate your private foundation status under § 507(a)(1).

You have made the following representations. You have not notified the Secretary of your intention to terminate your status as a private foundation. You, the Foundations, and your respective foundation managers have each represented that they have (i) made a full disclosure of the factual situation to the Service, (ii) made reasonable attempts to ascertain whether the transfers are a violation of Chapter 42, (iii) concluded that, to the best of their knowledge and information, the transfers are not violations of Chapter 42, and (iv) have not committed willful, repeated acts (or failures to act) or committed a willful and flagrant act (or failure to act) which gives rise to tax under Chapter 42. You have represented that the Foundations are effectively controlled, directly or indirectly, by the same person or persons who effectively control you within the meaning of § 1.507-3(a)(9) of the regulations. You do not currently have any outstanding grant that requires the exercise of expenditure responsibility within the meaning of § 4945(h) nor do you intend to make any such grants. You do not have any outstanding pledges and will allocate, pro rata, any charitable pledges made prior to your final distributions between the Foundations.

**Rulings Requested:**

You have requested the following rulings:

1. The proposed transfers to the Foundations will each constitute a "significant disposition of assets to one or more private foundations" within the meaning of § 1.507-3(a)(1) and (c).
2. The proposed transfers from you to the Foundations will not result in a termination of private foundation status under § 507(a), but will constitute a transfer between private foundations within the contemplation of § 507(b)(2).
3. The proposed transfers from you to the Foundations will not constitute either a notification of your intent to voluntarily terminate your status as a private foundation under § 507(a)(1), or "willful repeated acts (or failures to act) or a willful and flagrant act (or failure to act)," within the meaning of § 507(a)(2) such that you will, therefore, not be subject to tax under § 507(c).
4. The proposed transfers to the Foundations will not give rise to any investment income under § 4940.
5. The proposed transfers to the Foundations will not constitute self-dealing transactions and will not be subject to excise tax under § 4941.
6. You will not have any obligation to satisfy the minimum distribution requirements under § 4942 for the taxable year of the transfers.
7. The proposed transfers from you to the Foundations will not constitute jeopardizing investments for purposes of § 4944.
8. The proposed transfers from you to the Foundations will not constitute taxable expenditures under § 4945(d), and you will not be required to exercise expenditure responsibility under § 4945(h) with respect to the proposed transfers.

**Law:**

Section 501(c)(3) provides an exemption from federal tax for organizations that are organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 507(a)(1) states that a private foundation may voluntarily terminate its private foundation status by notifying the Secretary of its intention to voluntarily terminate its private foundation status pursuant to § 507(a)(1) and by paying any termination tax under § 507(c).

Section 507(a)(2) states that an organization's private foundation status may be involuntarily terminated by the Secretary if there have been either willful repeated acts (or failures to act), or a willful and flagrant act (or failure to act), giving rise to liability for tax under Chapter 42, and the Secretary notifies such organization that, by reason of these acts, such organization is liable for the tax imposed by subsection 507(c), and either such organization pays the tax imposed by subsection 507(c) (or any portion not abated under subsection 507(g)) or the entire amount of such tax is abated under subsection 507(g).

Section 507(b)(2) states that, in the case of a transfer of assets of any private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization, the transferee private foundation shall not be treated as a newly created organization.

Section 507(c) imposes on an organization that voluntarily terminates its private foundation status an excise tax equal to the lower of (1) the aggregate tax benefits that have resulted from the private foundation's exempt status under § 501(c)(3), or (2) the value of the net assets of the private foundation.

Section 507(d)(1) states that, for purposes of subchapter (c), the aggregate tax benefit resulting from the § 501(c)(3) status of any private foundation is the sum of (A) the aggregate increases in tax under chapters 1, 11, and 12 which would have been imposed with respect to all substantial contributors to the foundation if deductions for all contributions made by such contributors to the foundation after February 28, 1913, had been disallowed, and (B) the aggregate increases in tax under Chapter 1 which would have been imposed with respect to the income of the private foundation for taxable years beginning after December 31, 1912, if (i) it had not been exempt from tax under § 501(a), and (ii) in the case of a trust, deductions under § 642(c) had been limited to 20 percent of the taxable income of the trust (computed without the benefit of § 642(c) but with the benefit of § 170(b)(1)(A)), and (C) interest on the increases in tax determined under subparagraphs (A) and (B) from the first date on which each such increase would have been due and payable to the date on which the organization ceases to be a private foundation.

Section 4940 imposes on each private foundation which is exempt from taxation under § 501(a) for the taxable year, with respect to the carrying on of its activities, a tax equal to two percent of the net investment income of such foundation for the taxable year.

Section 4940(e) provides for a reduction in the excise tax on net investment income to one percent where a private foundation meets certain distribution requirements.

Section 4941(a) imposes an excise tax on acts of self-dealing between a private foundation and any of its disqualified persons as defined in § 4946.

Section 4942 imposes on the undistributed income of a private foundation for any taxable year, which has not been distributed before the first day of the second (or any succeeding) taxable year following such taxable year (if such first day falls within the taxable period), a tax equal to

30 percent of the amount of such income remaining undistributed at the beginning of such second (or succeeding) taxable year.

Section 4942(c) states the term "undistributed income" means, with respect to any private foundation for any taxable year as of any time, the amount by which--(1) the distributable amount for such taxable year, exceeds (2) the qualifying distributions made before such time out of such distributable amount.

Section 4942(i) adjusts the distributable amount where distributions during prior years have exceeded income. If, for the taxable years in the adjustment period for which an organization is a private foundation, (A) the aggregate qualifying distributions treated as made out of undistributed income for such taxable years or as made out of corpus during such taxable years, exceed (B) the distributable amounts for such taxable years, then, for purposes of this section, the distributable amount for the taxable year shall be reduced by an amount equal to such excess.

Section 4944(a) imposes a tax on any investment that jeopardizes any exempt purpose of a § 501(c)(3) private foundation.

Section 4945(a) imposes a tax on each taxable expenditure, payable by the private foundation. In addition, § 4945(a)(2) imposes a tax on each foundation manager who agrees to make a taxable expenditure unless that agreement is not willful and is due to reasonable cause.

Section 4945(d)(4) defines, in part, the term "taxable expenditure" to mean any amount paid or incurred by a private foundation as a grant to an organization unless the private foundation exercises expenditure responsibility with respect to such grant in accordance with subsection (h).

Section 4945(h) states that the term "expenditure responsibility" means that a private foundation is responsible to exert all reasonable efforts and to establish adequate procedures--(1) to see that a grant is spent solely for the purpose for which made, (2) to obtain full and complete reports from the grantee on how the funds are spent, and (3) to make full and detailed reports with respect to such expenditures to the Secretary.

Section 4947(a)(2) states that in the case of a trust which is not exempt from tax under § 501(a), not all of the unexpired interests in which are devoted to one or more of the purposes described in § 170(c)(2)(B), and which has amounts in trust for which a deduction was allowed under §§ 170, 545(b)(2), 642(c), 2055, 2106(a)(2), or 2522, § 507 (relating to termination of private foundation status), § 508(e) (relating to governing instruments) to the extent applicable to a trust described in this paragraph, § 4941 (relating to taxes on self-dealing), § 4943 (relating to taxes on excess business holdings) except as provided in subsection (b)(3), § 4944 (relating to investments which jeopardize charitable purpose) except as provided in subsection (b)(3), and § 4945 (relating to taxes on taxable expenditures) shall apply as if such trust were a private foundation.

Section 1.507-3(a)(5) states that, except as provided in subparagraph (9) of that paragraph, a private foundation is required to meet the distribution requirements of § 4942 for any taxable year in which it makes a § 507(b)(2) transfer of all or part of its net assets to another private foundation.

Section 1.507-3(a)(6) states that for purposes of § 4943(c)(4), (5), and (6), whenever a private foundation makes a § 507(b)(2) transfer of all or part of its net assets to another private foundation, the applicable period of time described in § 4943(c)(4), (5), or (6) shall include both the period during which the transferor foundation held such assets and the period during which the transferee foundation holds such assets.

Section 1.507-3(a)(9)(i) states that If a private foundation transfers all of its net assets to one or more private foundations which are effectively controlled (within the meaning of § 1.482-1(a)(3)), directly or indirectly, by the same person or persons which effectively controlled the transferor private foundation, for purposes of Chapter 42 (§ 4940 *et seq.*) and part II of subchapter F of Chapter 1 (§§ 507 through 509), such a transferee private foundation shall be treated as if it were the transferor. However, where proportionality is appropriate, such a transferee private foundation shall be treated as if it were the transferor in the proportion which the fair market value of the assets (less encumbrances) transferred to such transferee bears to the fair market value of the assets (less encumbrances) of the transferor immediately before the transfer. Subdivision (ii) states that subdivision (i) of this subparagraph shall not apply to the requirements under §§ 6033 and 6104, which must be complied with by the transferor private foundation, nor to the requirement under § 6043 that the transferor file a return with respect to its liquidation, dissolution, or termination.

Section 1.507-3(c)(1) states that a transfer of assets is described in § 507(b)(2) if it is made by a private foundation to another private foundation pursuant to any liquidation, merger, redemption, recapitalization, or other adjustment, organization, or reorganization, which includes any other significant disposition of assets to one or more private foundations.

Section 1.507-3(c)(2) defines the term "significant disposition of assets to one or more private foundations" as any disposition or series of dispositions where the cumulative total of the dispositions is 25 percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year.

Section 1.507-3(d) states that unless a private foundation voluntarily gives notice pursuant to § 507(a)(1), a transfer of assets described in § 507(b)(2) will not constitute a termination of the transferor's private foundation status under § 507(a)(1). Such a transfer must, nevertheless, satisfy the requirements of any pertinent provisions of Chapter 42. See subparagraphs (5) through (7) of § 1.507-3(a). However, if such transfer constitutes an act or failure to act which is described in § 507(a)(2)(A), then such transfer will be subject to the provisions of § 507(a)(2) rather than § 507(b)(2).

Section 1.507-4(b) states that private foundations that make transfers described in § 507(b)(2) are not subject to the tax imposed under § 507(c) with respect to such transfers unless the provisions of § 507(a) become applicable.

Section 53.4940-1(d) of the excise tax regulations states that, for purposes of paragraph (c) of that section, "gross investment income" means the gross amounts of income from interest, dividends, rents, and royalties received by a private foundation from all sources.

Section 53.4940-1(f) of the excise tax regulations provides rules for determining capital gain net income (net capital gain for taxable years beginning before January 1, 1977) for purposes of the tax imposed by § 4940.

Section 53.4946-1(a)(8) of the excise tax regulations states that, for purposes of § 4941 only, the term "disqualified person" shall not include any organization which is described in § 501(c)(3) (other than an organization described in § 509(a)(4)).

Rev. Rul. 2002-28, 2002-1 C.B. 941, rules on the implications of § 507(b)(2) transfers under §§ 4940, 4941, 4942, 4943, 4944, and 4945 for private foundations in various situations.

### **Analysis:**

Of your three directors, one sibling has a differing charitable philosophy and divergent charitable goals from the other two siblings. Accordingly, the proposed transfers are part of a larger transaction to distribute the marital and unitrust assets to the Foundations, so that the two sibling groups can direct the respective investment and exempt uses of those assets independent of the other.

### **Rulings 1, 2, and 3:**

Section 507(b)(2) describes a transfer from one private foundation to another private foundation according to any liquidation, merger, redemption, recapitalization, or other adjustment, organization or reorganization. Section 1.507-3(c)(1) describes the terms "other adjustment, organization, or reorganization" as including any partial liquidation or any other significant distribution of assets to one or more private foundations, other than transfers for full and adequate consideration or distributions out of current income. The term "significant disposition of assets to one or more private foundations" is defined by § 1.507-3(c)(2) as any disposition or series of dispositions where the aggregate value transferred is 25 percent or more of the fair market value of the net assets of the foundation at the beginning of the taxable year. Since you are transferring all of your assets to the Foundations, for no consideration, and not out of current income, your proposed transfers will qualify as a significant disposition of assets under § 507(b)(2).

Pursuant to § 1.507-4(b), a private foundation that makes a transfer described in § 507(b)(2) is not subject to the tax imposed under § 507(c) with respect to such transfer. However, § 507(a) states that the status of any organization as a private foundation shall be terminated only if the organization notifies the Secretary of its intent to accomplish such termination or, with respect to the organization, there have been either willful repeated acts (or failures to act), or a willful and flagrant act (or failure to act), giving rise to liability for tax under Chapter 42, and the Secretary notifies such organization that, by reason of § 507(a)(2)(A), such organization is liable for the tax imposed by § 507(c). As discussed in the paragraph above, your transfers will constitute a significant distribution of assets described in § 507(b)(2). You have not notified the Secretary of your intent to terminate your status as a private foundation, and you have not committed willful repeated acts (or failures to act) or committed a willful and flagrant act (or failure to act) which gives rise to tax under Chapter 42. Therefore, your proposed transfers of assets to the Foundations under § 507(b)(2) will not constitute either a notification of your intent to voluntarily terminate your status as a private foundation under § 507(a)(1), or "willful repeated acts (or failures to act) or a willful and flagrant act (or failure to act)," within the meaning of § 507(a)(2) such that you will

therefore not be subject to tax under § 507(c). The proposed transfers also will not terminate your private foundation status under § 507(a) but will constitute a transfer between private foundations within the contemplation of § 507(b)(2).

Ruling 4:

Section 4940 imposes a two-percent excise tax on the investment income of a private foundation. Sections 53.4940-1(d) and (f) state that gross investment income includes interest, dividends, rents, royalties, and capital gains from the sale or other disposition of property held for investment purposes. Your transfers to the Foundations, which lack consideration and are not out of current income, will not constitute investments or sales or other dispositions of investment property, which would generate investment income subject to excise tax under § 4940. Therefore, the transfers will not give rise to net investment income subject to tax under § 4940(a).

Ruling 5:

Section 4941(a) imposes an excise tax on each act of self-dealing between a disqualified person and a private foundation. Under § 53.4946-1(a)(8), a "disqualified person" does not include organizations that are exempt under § 501(c)(3). Accordingly, because the Foundations are recognized by the Service as organizations exempt under § 501(c)(3), your transfers to the Foundations will not be acts of self-dealing and will not be subject to the excise tax under § 4941.

Ruling 6:

Section 4942 generally imposes an excise tax on the undistributed income of a private foundation (other than an operating foundation under § 4942(j)(3)) for any taxable year. Since you are transferring all of your assets to the Foundations, which you represent are effectively controlled by the same persons who control you, the Foundations will be treated as though they were you for that taxable year under § 1.507-3(a)(9)(i). Therefore, for the taxable year of the transfers, the Foundations will assume all obligations with respect to your "undistributed income" within the meaning of § 4942(c), if any, and succeed to the amount of your excess qualifying distributions under § 4942(i), using proportionality as appropriate, in accordance with § 1.507-3(a)(9)(i). Accordingly, you will not have any obligation to satisfy the minimum distribution requirements under § 4942 for the taxable year of the transfers.

Ruling 7:

Section 4944 imposes an excise tax on investments that jeopardize a private foundation's charitable purpose. In Ruling 4 above, we determined that your transfers to the Foundations, which will lack consideration and will not be out of current income, will not constitute investments or sales or other dispositions of investment property. Therefore, as explained in Rev. Rul. 2002-28, *supra*, your transfers to the Foundations will not constitute investments that jeopardize your exempt purposes and will not be subject to tax under § 4944.

Ruling 8:

Section 4945(d) imposes an excise tax on each taxable expenditure made by a private foundation as a grant to an organization unless the private foundation exercises expenditure

responsibility with respect to the grant in accordance with subsection (h). However, since you will transfer all of your assets to the Foundations, which you represent are effectively controlled, directly or indirectly, by the same persons that effectively control you, for purposes of Chapter 42, the Foundations will be treated as if they were you. Because the Foundations will be treated as if they were you rather than as recipients of expenditure responsibility grants, there will be no expenditure responsibility requirements that must be exercised under § 4945(d)(4) or (h) with respect to your transfers to the Foundations. See Rev. Rul. 2002-28, *supra*.

Conclusion:

Based on the foregoing, we rule as follows:

1. The proposed transfers from you to the Foundations will each constitute a "significant disposition of assets to one or more private foundations" within the meaning of § 1.507-3(a)(1) and (c).
2. The proposed transfers from you to the Foundations will not result in a termination of private foundation status under § 507(a), but will constitute transfers between private foundations as described in § 507(b)(2).
3. The proposed transfers from you to the Foundations will not constitute either a notification of your intent to voluntarily terminate your status as a private foundation under § 507(a)(1), or "willful repeated acts (or failures to act) or a willful and flagrant act (or failure to act)", as described in § 507(a)(2). Therefore, you will not be subject to tax under § 507(c).
4. The proposed transfers from you to the Foundations will not give rise to any net investment income under § 4940.
5. The proposed transfers from you to the Foundations will not constitute self-dealing transactions and will not be subject to excise tax under § 4941.
6. You will not have any obligation to satisfy the minimum distribution requirements under § 4942 for the taxable year of the transfers.
7. The proposed transfers from you to the Foundations will not constitute jeopardizing investments for purposes of § 4944.
8. The proposed transfers from you to the Foundations will not constitute taxable expenditures under § 4945(d), and you will not be required to exercise expenditure responsibility under § 4945(h) with respect to the proposed transfers.

This ruling will be made available for public inspection under § 6110 after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.



If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Theodore R. Lieber  
Manager, Exempt Organizations  
Technical Group 3

Enclosure  
Notice 437